

Anglo American (AGLJ.J)

Alert: More acquisitions: this time met coal

Anglo American announced that it will buy a 58.9% interest in Revuboe metallurgical coal property in Mozambique for a cash consideration of A\$540 mn from Talbot Estate. The other partners to the project are Nippon Steel Corporation (33.3%), and POSCO (7.8%). The acquisition price is relatively small at about 1.3% of Anglo's Market cap. However, significant capex may be required to complete the project.

Revuboe is being developed as an open pit mine in Moatize Basin of Mozambique with expected first production from September 2013 as per the project website. The project has JORC resources of 1.4 billion tonnes of hard coking and thermal coal that has potential to export 6-9 Mt annually on 100% basis.

Vale is already developing its Moatize coal project in the same region with estimated capital outflow of ~\$2.1bn for a capacity of 11 million tons, (70% coking coal and 30% thermal). Vale will spend another \$4.4 bn to develop rail and port infrastructure to facilitate shipments from the mine.

We believe that this transaction is negative for Anglo given: 1) Anglo owns enough met coal resources in Australia and Canada, where it already has scale. It has Grosvenor 1 and 2 and Moranbah South as well as Peace River Coal in Canada. 2) The project still needs to be completed, which means there is execution risk. Met coal projects could cost up to \$400 per annual production tonne to complete, so lots of cash to be spent still. 3) We would have preferred a share buy back or dividends given Anglo's cheap valuation and low payout ratio. 4) Chinese steel consumption could fall over the coming years putting significant pressure on steelmaking materials— for more details refer to [China Rebalance - The Impact On Steel](#).

On positive side Anglo is focusing on its core operations and its past experience as a successful operator in African continent might add value to the project. The deal could add potentially 3.5-5.3 Mt of coal production annually to Anglo's share of production.

BUY rated — We maintain our Buy on Anglo but continued capital spend on acquisitions above our NPV (Kumba and Minas Rio) and which limits dividend yield could erode our positive stance. The company should continue to benefit from volume growth in 2012 as three major projects (Kolomela, Los Bronces and Barro Alto) are ramping up. We believe Minas Rio, Anglo Sur and Angloplat disappointments are now well understood and largely priced in. We calculate a total one-year return of 32% to our target price of R330 and maintain Anglo's South African listing as Buy.

Company Update

Buy	1
Price (24 Jul 12)	R256.79
Target price	R330.00
Expected share price return	28.5%
Expected dividend yield	2.7%
Expected total return	31.2%
Market Cap	R356,979M
	US\$42,194M

Price Performance

(RIC: AGLJ.J, BB: AGL SJ)



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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Anglo American

Valuation

Our R330 target price for Anglo is based on a 50/50 weighting of our DCF fair value of R376 and a P/E derived value of R280, whereby we apply a 8x PE multiple to 2013E earnings (a 20% discount to Anglo's long-term average of 10.3x to offset 2013's above average margin forecast and to reflect significantly increased capex spend). We derive our DCF valuation based on: 1) a weighted average cost of capital (WACC) of 9.52%; 2) long-term (2013-23E) nominal revenue growth of 5% per annum; 3) long-term EBITDA margins of 33%; 4) a long-term capex/EBITDA ratio of 41%; 5) long-term ROCE of 16%; and 6) a terminal growth rate (after 2023E) of 3.5% (implying an exit P/E multiple of 11.6x).

Risks

The biggest risks to our earnings forecasts and valuation relate to our commodity price and currency forecasts.

Industry-specific risks include government actions, such as controls on imports, exports and prices, new forms or rates of taxation and royalties, and increased government regulation. South African miners started paying mining royalties in March 2010, in line with global best practice and market expectations.

Higher-than-forecast inflation in the mining sector could lead to near-term margin compression, but should support higher commodity prices in the long term.

Skills, electricity and water shortages in South Africa may affect production and mining inflation more than we anticipate. As around 40% of Anglo's assets are in South Africa, this could erode Anglo's global competitiveness.

Over-estimation of mineral reserves could weaken our investment case. We assume long-term reserve replacement at a fixed capital cost to EBITDA. Failure to discover new reserves or expand existing reserves could therefore impact on Anglo's valuation.

Conversely, if any of these factors proves to have less of an effect than we anticipate, the stock could materially outperform our target.

Appendix A-1

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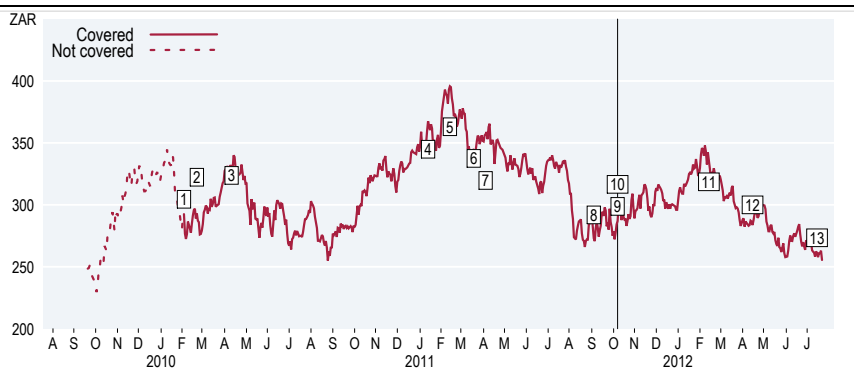
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Anglo American (AGLJ.J)

Ratings and Target Price History Fundamental Research

Analyst: Johann Pretorius

Covered since February 4 2010



	Date	Rating	Target Price	Closing Price
1	3-Feb-10	*1M	*340.00	292.50
2	22-Feb-10	1M	*360.00	293.00
3	12-Apr-10	1M	*420.00	328.50
4	13-Jan-11	1M	*430.00	367.50
5	14-Feb-11	*2M	*450.00	395.70

* Indicates change

	Date	Rating	Target Price	Closing Price
6	18-Mar-11	*1M	450.00	344.42
7	5-Apr-11	1M	*460.00	357.10
8	5-Sep-11	1M	*420.00	273.00
9	7-Oct-11	Stock rating system changed		
10	7-Oct-11	*1	420.00	286.93

	Date	Rating	Target Price	Closing Price
11	14-Feb-12	*2	*380.00	335.60
12	16-Apr-12	*1	*360.00	283.68
13	16-Jul-12	1	*330.00	261.20

Rating/target price changes above reflect Eastern Standard Time

Anglo American (AGLJ.J)

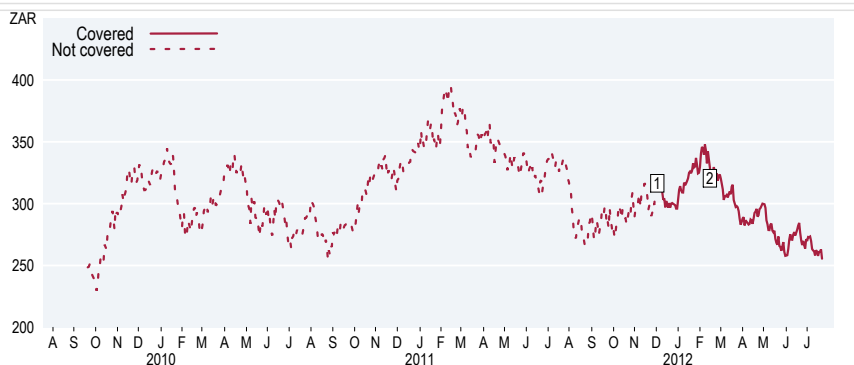
Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Johann Pretorius

Covered since February 4 2010



	Date	Rating	Target Price	Closing Price
1	2-Dec-11	*ADD MP	-	311.28

* Indicates change

	Date	Rating	Target Price	Closing Price
2	15-Feb-12	*REM MP	-	329.21

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Data current as of 30 Jun 2012

	12 Month Rating			Relative Rating		
	Buy	Hold	Sell	Buy	Hold	Sell
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